PEPSICO, INC. ANNUAL REPORT 1966

PepsiCo, Inc. is a world-wide consumer products and service company whose divisions specialize in soft drinks, convenience foods, and leasing services. As a corporate management entity it performs strategic planning, establishes uniform policies, and provides specialized services for its divisions, but each division is responsible for the operation of its own affairs to maximize the return on financial and other resources employed in its operation. Through its divisions the company has product or service representation in 111 countries.

CONTENTS

TO OUR SHAREHOLDERS:

We are indeed pleased to report to you that in 1966 in both sales and earnings PepsiCo, Inc. broke all previous records.

Net sales rose to $604,665,701 for the year ended December 31, 1966, as compared with $509,950,282 for 1965, an increase of 19 percent.

For the same period, your Company's net income after taxes rose to $38,040,288 from $33,199,301 in 1965. Converted to a per share basis, this amounted to $3.65 on 10,421,763 shares of stock outstanding at the end of 1966, compared to $3.21 on 10,330,990 shares outstanding at the end of 1965, an increase of 14 percent per share.

Especially outstanding and significant for the future was the growth in our Pepsi-Cola Division, PepsiCo International Division, and Frito-Lay Division. We continue to be optimistic about Lease Plan International Corp., whose acquisition in early 1966 was reported to you last year, and whose financial results are included separately herein. Empire State Sugar Company, plagued with many delays and problems, some still unresolved, operated at a loss; the decision was made to write down the value of this facility in the amount of $12,000,000, resulting in a charge to retained earnings of $6,240,000. These matters are described further in this Report, particularly in Note 2 on page 22.

On February 23, 1967, as widely reported in the press and other media, your Board of Directors voted to recommend to you for your approval at the Annual Meeting to be held in Wilmington, Delaware, on May 3, a two-for-one stock split. We also announced that Company management intends to recommend to the Board at its May meeting that the quarterly dividend, currently at the rate of 40 cents per share, be increased to 45 cents per share, which would be 22½ cents per share following the proposed two-for-one split. Details of the stock split are contained in the Proxy Statement, which is enclosed.

In pursuit of its record growth in 1966, your Company introduced new soft drink and convenience food products at home, opened new areas abroad, and entered into an agreement for the acquisition of North American Van Lines, which together with Lease Plan International Division will constitute our entry into the service industry. The acquisition, already approved by the Boards of both companies and ratified by North American Van Lines' stockholders as required, is subject to the approval of the Interstate Commerce Commission. Hearings have been held before the Commission, and a decision is now pending.

In light of changes in the tax laws which temporarily eliminate the seven percent investment tax credit and part of the allowance for accelerated depreciation, management has carefully reviewed all plans for capital investment in 1967. These changes in tax law will not, of course, postpone our investment in equipment essential to continued growth and consequent enhancement of your investment, such as trucks, vending equipment, production facilities, and other tools of progress. This program is not expected to require additional long-term financing.

In support of our purpose to continue lasting and profitable growth, we strengthened our management group with particular emphasis on developing promising young people for the future. The spirit and pride of accomplishment in our employees we respect and salute as our greatest asset.

Barring economic or other uncertainties over which we cannot exercise control, from our experience we have intelligent cause to anticipate another good year in 1967. As a diversified, international Company principally oriented to soft drinks and convenience foods, we are dedicated to continued growth through any or all channels which prove advantageous, including new products from our research facilities, new opportunities, new markets, and deeper penetration of existing markets. In addition, we are constantly alert to opportunities for lower costs and increased efficiency wherever they arise.

In all this, your management considers no operating figures more important than net income per share of outstanding stock.

The following pages report more fully on the year's developments in our various divisions.

Very truly yours,

Herman W. Lay
Chairman of the Board

Donald M. Kendall
President

March 14, 1967

President Kendall, Chairman Lay.

FINANCIAL HIGHLIGHTS

Net Sales in 1966 were $604,666,000, an increase of 19 percent over $509,950,000 in 1965.

Net Income for 1966 was $38,040,000, compared with $33,199,000 for the preceding year.

Earnings Per Share were $3.65, rising 14 percent from $3.21 in 1965.

Shares Outstanding at the end of 1966 were 10,421,763 and at the same time a year earlier were 10,330,990.

Dividends paid on common stock in both 1965 and 1966 were $1.60 per share, at the rate of 40 cents quarterly.

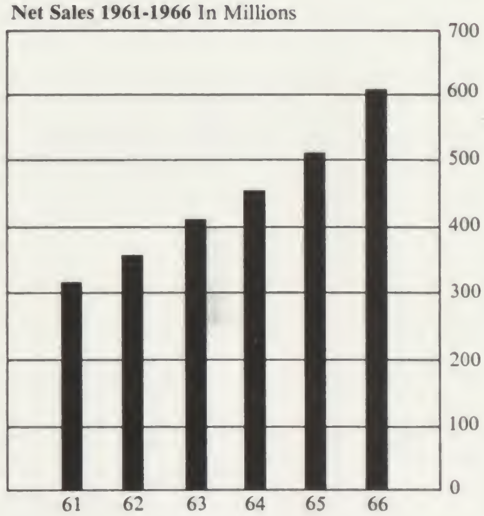
Total Property, Plant and Equipment increased $34,916,000 in 1966, in addition to $16,908,000 (net of a twelve million dollar write-down described in Note 2 on page 22) transferred from Lease Plan with respect to the Montezuma sugar facility.

Depreciation and Amortization was $16,470,000 and $13,770,000 for 1966 and 1965 respectively.

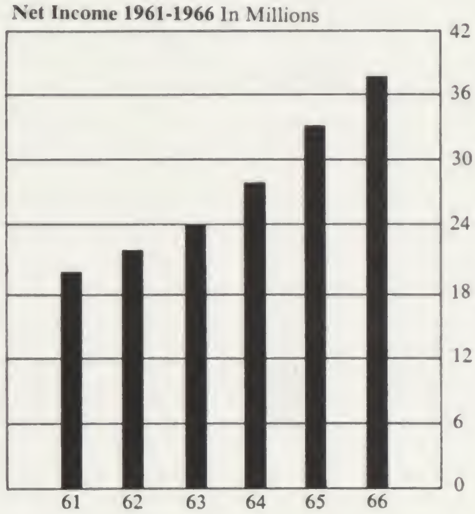
Shareholders' Equity increased to $192,214,000 at the end of 1966, compared with $170,448,000 a year earlier.

Book Value Per Share at the end of the respective years was $18.44 in 1966 and $16.50 in 1965.

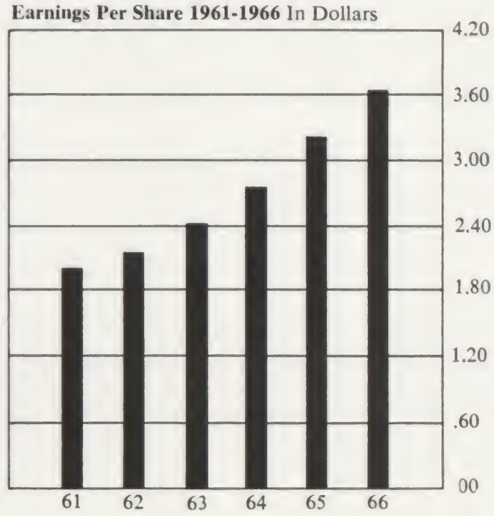
Net Sales 1961-1966 In Millions



Net Income 1961-1966 In Millions



Earnings Per Share 1961-1966 In Dollars



Peter K. Warren
President, PepsiCo International
James B. Somerall
President, Pepsi-Cola Company
William B. Oliver
President, Frito-Lay, Inc.

Case and dollar sales of Pepsi-Cola Company, responsible for PepsiCo's domestic soft drink business, reached record levels and continued to rise into the new year.

Sales of the principal product, Pepsi-Cola, reached an all-time high at a growth rate unsurpassed in a decade, and toward year's end trended sharply upward. Each of the Company's 10 sales regions showed an increase. Diet Pepsi-Cola, competing in a static market segment, nevertheless increased its sales substantially.

Sales of Mountain Dew, nationally advertised for the first time on three TV networks, continued to increase. The product is now available to 92 percent of the population. Teem sales declined, but less than the lemon-lime market segment of the industry. Patio flavors, which 21 new Bottlers added, recorded impressive gains.

In mid-September, within the area served by seven Pepsi plants in New York, New Jersey, and Pennsylvania, the Company introduced its new chocolate drink, Devil Shake. Public reception was most encouraging.

Convenience packages (cans and non-returnable bottles), cold cartons, vending, and fountain dispensers provided notable sales increases.

The Company's industry leadership in non-returnable bottles is such that Pepsi-Cola Bottlers serving two-thirds of the national population now market the product in one-way bottles. The number of Bottlers' canning facilities—currently 15—will be increased in 1967 to meet the growing popularity of canned products.

Pepsi-Cola Bottlers were outstandingly successful in placing Vis-A-Coolers—large refrigerated display units for 6-pack and 8-pack cartons. Sales of can-vending machines more than doubled those of any previous year. Aided perceptibly by syrup transfer tank and jugging programs, and by sales incentive programs, fountain sales rose sharply, as they had similarly done in 1965.

In early Fall the Company launched new, product-oriented national advertising campaigns for Pepsi-Cola ("Taste that beats the others cold—Pepsi pours it on") and Diet Pepsi-Cola ("The girls girl-watchers watch drink Diet Pepsi"). The former was introduced in full-page

High visibility, attractive display, and refrigeration help Vis-A-Coolers sell cold cartons in thousands of outlets.

PEPSI
Take home a carton
Cold
PEPSI
PEPSI PEPSI PEPSI
DEVIL SHAKE
Mountain Dew
Pepsi
DIET PEPSI
RICE KRISPIES

four-color ads in national magazines, and in prime-time TV spots on three networks. The Diet Pepsi campaign was launched in print and indoor and outdoor posters. On TV and radio, the new musical theme quickly caught the public ear, and within a few weeks various popular groups, including Al Hirt, Nelson Riddle, Les and Larry Elgart, and the Bob Crewe Generation, had recorded it for public sale under the title "Music to Watch Girls By."

Pepsi-Cola Metropolitan Bottling Company, Inc., the wholly-owned bottling subsidiary which operates 24 Pepsi-Cola bottling plants, registered the highest sales increases in a decade. In February the lengthy strike in New York City plants was settled, and Metropolitan began substantial recovery of its former sales level in these plants. In Flint, Michigan; Las Vegas, Nevada; and Phoenix, Arizona, plants were expanded as required by growth. The Company acquired the bottling plants in Jackson and Meridian, Mississippi, for the purpose of developing their sales.

New plants and large-scale additions were completed in 25 independent Bottler franchises at a cost exceeding eight million dollars, and more than nine million dollars of equipment was added to bottling plants.

As assistance to Bottlers the Company also conducted training meetings for over 500 route managers and 3,500 salesmen, and completed plans for a Pepsi-Cola Management Institute, a facility to give professional advanced training to Bottler and Company management—the first permanent installation for this purpose in the industry.

Highly successful conferences with Bottlers in the Fall introduced the 1967 marketing programs and again demonstrated the excellent state of communications between Bottlers and the Company. Pepsi-Cola Bottlers, demonstrating confidence in Company leadership and programs, invested more heavily in marketing tools than ever before.

During 1966, Samuel H. Desch was named Executive Vice President of Pepsi-Cola Company. The following men were promoted to Vice President: Wesley Astin (Executive Director of the Pepsi-Cola Management Institute); Charles de Charleroy (Southern Division); Benjamin U. Dugas (Sales Training); Alonzo H. England (Purchases); Raymond A. Helsel (Grocery and Mobile Market Sales); John C. Klett, Jr. (Administration); and Stephen J. Welsh (Planning). Elected Directors of Pepsi-Cola Company were D. Mitchell Cox and Herman A. Schaefer.

Every study of the soft drink industry indicates that its recent growth rate will continue to be enhanced by the predicted increase of personal income and leisure time, the introduction of additional products, and expanding population in the age brackets where per-capita consumption is highest. In this growing industry, Pepsi-Cola Company will continue its aggressive pursuit of growth.

Reinforcing a new theme for an old favorite, advertising visualizations emphasize the superior taste of Pepsi cold.


Pepsi

Forging ahead in the rapidly growing convenience foods industry, Frito-Lay again recorded historic new highs in sales and profits. Despite increased competition and abnormally low potato yields in the first half of the year, which affected earnings, financial growth and market volumes broke every past high record.

Lay's potato chips and Fritos corn chips again led the division's other products in sales volume, but a relatively new product, Doritos tortilla chips, surged vigorously ahead and achieved national distribution.

Other principal snack products contributing to the division's record volume were Ruffles potato chips, Chee·tos cheese puffs, Rold Gold pretzels, Baken-ets pork rinds, Lay's dry roasted peanuts, and Fritos brand dip mixes.

The convenience specialty foods of regional distribution, processed and marketed by Austex, Nu-Way, and Belle Products Divisions, grew in volume and market share. In the Southeast, Southwest, and contiguous areas, these divisions manufacture and distribute packaged specialties such as beef stew, spaghetti and meat balls, chili, tamales, olives, onions, peppers, and institutional servings

of jellies, mayonnaise, mustard, and relishes.

To support growth of various products Frito-Lay doubled the capacity of the snack foods plant in Houston, Texas; opened a new and highly modern pretzel plant in Canton, Ohio; installed a new processing line for corn chips in Montreal, Canada; and in Irving, Texas, adjacent to Dallas, completed construction of its largest production and research facility, a 220,000-square-foot complex. Its research and engineering facilities, covering 80,000 square feet, are the most advanced and comprehensive in the industry. Research is concentrated on new and improved products, processing and engineering equipment, and improvement in raw materials. Frito-Lay also operates in Rhinelander and Madison, Wisconsin, a genetics program dealing with the breeding of new and improved varieties of potatoes, corn, and other agricultural products it uses.

Response to the Company's advertising, regional and national, continued to be excellent. It was the recipient

The snack food industry's most advanced research facilities, as well as production lines and Southwestern zone and division field offices, are housed in Frito-Lay's new four-million-dollar complex just outside Dallas, Texas.

of many professional awards. Bert Lahr, famous comedian featured in the television campaign for Lay's potato chips, was named by American TV Festivals as the best TV spokesman of the year. The outdoor campaign for Lay's potato chips was selected as the best of the year. Other awards went to Doritos tortilla chips, Austex chili, and the outdoor campaign for Fritos corn chips.

The record of 1966 was made possible by the high competence, determination, and pride of the men and women who compose the Company. Their spirit is second to none. During the year three men were elevated to Vice President: Mr. Darrell Agee for the Northwest Division, Mr. Joseph Fields for Trade Relations, and Mr. Barney Hilton for Research.

Frito-Lay, the pioneer in developing a national snack foods business, created consumer demand for corn chips and has become the only company in the snack food industry manufacturing and distributing its brand of corn chips and potato chips on a nation-wide basis. More than any other company, it has contributed to building a snack foods market in the United States with industry sales which have helped stimulate such interest that many of the country's largest enterprises have entered the field and are continuing to enter it. This increased activity, together with the increase in population and leisure time, serves to expand the snack food market further and to increase competition.

Frito-Lay management, with an operating organization which has invaluable experience and know-how, has no doubt of its ability to maintain its leadership and continue to move ahead with this vibrant industry.

Opposite: Some of the many food items produced and sold by Frito-Lay, Inc., under Towie, Austex, and other brand names. Below: One of the prize-winning series of outdoor billboards for Lay's potato chips, featuring comedian Bert Lahr.


Towie
SPANISH OLIVES
AUSTEX
chili
WITHOUT BEANS
Towie
IMPORTED HOLLAND COCKTAIL ONIONS
Towie
IMPORTED ITALIAN PEPPERS
OPEN
CLOSE
"Twist-Off"
Towie
MILD BANANA PEPPERS
AUSTEX
spaghetti AND meatballs
WITH TOMATO SAUCE
Fritos
BEAN dip
Fritos
BACON-ONION
Fritos
ONION dip MIX
TWIN PACK
25¢
Fritos
GREEN ONION dip MIX
TWIN
AUSTEX
beef stew
Towie
ARTICHOKE HEARTS
Towie
GIANT RIPE OLIVES
OPEN
Refrigerator Jar
CLOSE
NEW "Twist-Off" CAP
Towie
SPANISH OLIVES
PIMIENTO STUFFED
MEXENE
MEXENE
CLOSE
OPEN
"Twist-Off"
Towie
MARASCHINO CHERRIES
Fritos
Jalapeño BEAN dip

In the first full year since its organization as a division of PepsiCo, Inc., PepsiCo International lifted product sales to new heights around the world, exceeding every previous achievement in sales and income.

Each of the six Area operations—Canada, Europe, Latin America, the Middle East, Southern Africa and the Far East including Australia—is now well organized to make its own timely operating decisions. Each area gained in sales volume and profit contributions during the year.

Beverages. Consumer acceptance of both Pepsi-Cola and Company flavors continued to show gains in 1966 throughout all operating areas. The sales of flavors—including Mirinda, Paso de los Toros tonic water, Teem, Mountain Dew and Guarinda (a flavor created for the Brazilian market)—almost doubled those of the previous year and now account for approximately 10 per cent of PepsiCo International's soft drink sales. In the three-year period since December, 1963, sales volume in International markets has increased by approximately 50 per cent.

During 1966, 50 Bottlers in 13 countries introduced one or more of our flavors, bringing the total flavor Bottlers to 226 in 44 countries. Mountain Dew in its first introductions outside the United States enjoyed successful acceptance in Canada and South Africa. Also during the year Pepsi-Cola became the first American soft drink to be sold in Yugoslavia, and for the first time was bottled in Belgium and Austria. In addition, during the year 15 other new bottling plants were opened through independent Bottlers or the Company in Chile, Venezuela, Argentina, Mexico, Germany, South Africa, Japan, Ethiopia, Brazil, and Jamaica.

At year's end there were 472 Pepsi-Cola plants in 110 countries and territories outside the U.S.A. PepsiCo International, which through its subsidiary companies now owns and operates 31 bottling plants in nine countries, acquired two bottling plants in Europe—Cologne, Germany, and Rome, Italy—where the Company's products will be aggressively promoted. Operation of the Rome plant began in January, 1967. Through the Company-owned bottling operation in Buenos Aires, Pepsi-Cola, Mirinda, and Paso de los Toros tonic water have enjoyed outstanding consumer acceptance. Increasing demand required construction of a second bottling plant in Buenos Aires during the year, and plans are under way for building a third plant in 1967.

Convenience Foods. With the acquisition of a major interest in a snack food company in Japan, the Company now has total or partial equity in food operations in six major markets outside the U.S.A.—Japan, Mexico, Canada, the United Kingdom, West Germany, and Austria—and has a franchise in South Africa. A new manufacturing facility for the production of snack foods is being built for the Mexican markets. The plants in England have been reorganized and modernized to increase both the quality and quantity of products for that market. To speed up the development of the Company's food products overseas, a new specialized department has been staffed with experienced personnel in the food industry. This group will give particular emphasis to associations with going businesses in Europe, Latin America, and the Far East, areas that now appear the most promising for the development of food products.

The greatest exposure of PepsiCo advertising continued to be at local levels, where mass media vehicles such as television, radio, cinema, print, and outdoor and indoor displays were used to good advantage by both the Company and franchised Bottlers. In addition, advertising of PepsiCo products—particularly Pepsi-Cola—through international media printed in 12 languages reached 45 million readers in over 110 countries.

In furtherance of its programs of public exposure, the Company sampled both food and beverage products in trade fairs and exhibits in a number of countries; completed arrangements for major participation in the 1967 World's Fair (Expo 67) to be held in Montreal; and continued its support of ACCION with Bottlers in Venezuela and Brazil, and of the Community Development Program of the International Junior Chamber of Commerce.

The realistic, aggressive plans guiding each operating unit of International in 1967 bid to make this a most satisfactory year for increased sales, and one of expansion for both soft drinks and food items in present and new areas.

In 1967 Pepsi-Cola—and wherever possible, flavors also—will be introduced into six new countries, among them Rumania. All in all, some 15 or 20 new bottling plants will go into operation in Yugoslavia, Brazil, the Philippines, Turkey, Venezuela, Argentina, and other countries, including some where negotiations are currently in progress for Bottler appointments.

Negotiations are now in progress to acquire existing food companies in two or three countries and to form a joint venture with local business in others for the manufacture and distribution of food products. None of these negotiations has been completed, but it will be the aim of PepsiCo International management to pursue aggressively its program for entering the food field in several countries overseas in 1967.

A Moroccan who sells water to others buys Pepsi for himself.

Consolidation and growth marked the year 1966 for Lease Plan International Corp. LPI probed for new and more profitable methods of doing business consonant with its general operating philosophy.

During the year its Finance Lease Division contracted for more than 20,000 additional vehicles. New clients, some of whose names are listed below,* illustrate the remarkable acceptance its programs enjoyed.

LPI is presently the nation's largest lessor of large fleets of trucks, and this recently revamped Truck Leasing Division is now planning an aggressive campaign to increase its volume to a substantial degree. Its sales force has been augmented, and new sales aids are in the process of development. Originally confined to a small area in the Northeast, the Truck Leasing Division is now established with additional self-sustaining operations in Kentucky, Michigan, Missouri and Illinois, and is moving in the direction of national coverage. All of the operations of this division are on customers' premises (there are no central garages) and the division owns no vehicles that are not on full-time lease.

In 1966, ventures into an LPI used car auction and a retail used car center, both in Los Angeles, proved unprofitable and were terminated in November. These discontinued operations contributed in substantial measure to the decline in the pre-tax profits of LPI. In addition, after-tax profits were adversely affected by the elimination of the investment credit in October, 1966.

The recent signs of relaxation in the extremely tight mortgage money market augurs well for the National Trailer Convoy Division, whose rapid growth was somewhat slowed by the lack of available consumer financing for the new mobile homes it transports. The Company's ability to meet the growing demand for the transportation of prefabricated buildings and components was increased late in the year by the addition of Whitehouse Trucking, Inc., of Toledo, Ohio.

A new Executive-type car leasing operation in Camden, New Jersey (a joint venture) is progressing satisfactorily but is not expected to contribute to profits until early 1967.

In 1966, LPI's Mobilease Division – a supplier of school buildings, laboratories, bank buildings, office and production facilities–produced a modest profit after losses during its first two years of operation. Much publicity has attended the rapidity with which this kind of structure is built today. One such building, of 10,000 square feet, was completed and made ready for occupancy only seven weeks after the contract was received. The engineering and sales staff of Mobilease provides specifications for these structures, but other plants are engaged to fabricate the units. The rapid acceptance of these structures encourages study of the possibilities of expanding to areas other than the West Coast.

The franchising of new car dealers as part of the Executive Car Leasing System continues to expand, although hampered by the recent lack of available financing.

Activities in Canada, Puerto Rico, Japan and South Africa are operating profitably and are expanding.

It is anticipated that the year 1967 will show all-time records in volume and profit.

Lease Plan International, the services division of PepsiCo, will remain on the alert for new opportunities in which to expand in the burgeoning service industry.

**New Client List:* American Can Company, Champion Paper, Inc., Continental Can Corporation, Cutler-Hammer, Inc., Gulfstan Corporation, Humble Oil & Refining Company, International Minerals & Chemicals Corp., Kelsey Hayes Corporation, Quaker State Oil Company, A. O. Smith Corporation, Sperry Rand Corporation.

The Company's new combination beet/cane sugar plant in central New York State refined approximately 100,000 cwt. of sugar from approximately 6,000 acres of beets harvested during the latter part of 1966. It is expected that the plant will commence refining raw cane sugar for the first time early this Spring. When the facility is complete and operable, it will be capable of producing an aggregate of 2,000,000 cwt. of refined sugar per year from both beet and cane.

As previously brought to your attention, particularly in PepsiCo's periodic reports to shareholders, this project has not been without serious problems. The dispute with the contractor, who was required by agreement to deliver a complete and operable plant no later than September 30, 1965, for a maximum guaranteed cost, continues, and the Company's ultimate claim against the contractor will total several millions of dollars.

Your attention is specifically called to Note 2 to the Financial Statements (page 22) of this report, which describes in some detail the accounting treatment which the Company has applied to a write-down of accumulated excessive costs of the facility to a more realistic figure, and to the operating loss of 1966.

While improvement is expected, present forecasts are that additional losses will be incurred in 1967. The Company will, of course, continue to keep its shareholders informed.

ARTHUR YOUNG & COMPANY

277 PARK AVENUE
NEW YORK, N.Y. 10017

The Board of Directors and Shareholders,
PepsiCo, Inc.

We have examined the accompanying consolidated balance sheet of PepsiCo, Inc. and subsidiaries at December 31, 1966 and the related consolidated statement of income and retained earnings for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the statements mentioned above present fairly the consolidated financial position of PepsiCo, Inc. and subsidiaries at December 31, 1966 and the consolidated results of their operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Arthur Young & Company

March 10, 1967

PepsiCo, Inc. and Subsidiaries

CONSOLIDATED STATEMENT OF INCOME AND RETAINED EARNINGS Years ended December 31, 1966 and 1965

	1966	1965
REVENUES		
Net sales	$604,665,701	$509,950,282
Interest and other income	4,815,920	2,193,036
Equity in income of Lease Plan International Corp.	3,389,406	3,706,199
	612,871,027	515,849,517
COSTS AND EXPENSES		
Cost of sales	287,611,009	234,618,140
Advertising, selling and administrative	250,298,353	215,740,763
Interest expense	4,395,832	1,618,867
Other expenses	4,720,545	5,608,546
	547,025,739	457,586,316
Income before federal and foreign income taxes	65,845,288	58,263,201
Provision for federal and foreign income taxes (including deferred 1966—$1,456,000; 1965—$1,278,900)	27,805,000	25,063,900
Net income	38,040,288	33,199,301
Retained earnings at beginning of year	134,582,460	119,306,772
Cash dividends—$1.60 per share in each year	(16,620,593)	(14,243,519)
Dividends of pooled companies prior to merger	—	(3,364,140)
Write-down of sugar facility (net of federal income tax benefit) (Note 2)	(6,240,000)	—
Other	—	(315,954)
Retained earnings at end of year	$149,762,155	$134,582,460

See accompanying notes.

PepsiCo, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEET December 31, 1966 and 1965

ASSETS	1966	1965
CURRENT ASSETS		
Cash	$ 29,634,594	$ 15,810,268
Short-term securities (approximates market)	46,538,479	27,036,450
Notes and accounts receivable, less allowance	40,728,422	34,219,161
Inventories—at cost (principally average method) not in excess of market	53,965,385	44,468,622
Prepaid expenses	8,046,262	7,455,922
	178,913,142	128,990,423
INVESTMENTS AND LONG-TERM RECEIVABLES		
Lease Plan International Corp.—at equity	15,466,931	15,267,181
Receivables (non-current) and other investments (at cost less reserves)	10,928,414	11,223,214
	26,395,345	26,490,395
PROPERTY, PLANT AND EQUIPMENT, AT COST		
Land	8,825,522	8,285,757
Buildings	40,639,312	34,002,635
Machinery and equipment	165,024,582	125,873,115
Bottles and cases	22,642,299	17,146,520
	237,131,715	185,308,027
Less accumulated depreciation and amortization	89,335,175	75,569,873
	147,796,540	109,738,154
OTHER ASSETS	12,732,431	6,229,815
	$365,837,458	$271,448,787

See accompanying notes.

LIABILITIES AND SHAREHOLDERS' EQUITY	**1966**	1965
CURRENT LIABILITIES		
Notes payable (including current installments on long-term debt)	**$ 20,775,527**	$ 12,199,417
Accounts payable and accrued liabilities	**51,471,950**	44,386,132
Federal and foreign income taxes	**18,526,202**	12,237,958
Customers' deposits on bottles and cases	**11,356,387**	8,387,753
	102,130,066	77,211,260
LONG-TERM DEBT	**69,393,425**	17,830,590
DEFERRED FEDERAL INCOME TAXES	**2,100,000**	5,958,563
SHAREHOLDERS' EQUITY		
Capital stock, par value 33⅓¢ per share; authorized 12,000,000 shares; issued and outstanding at December 31, 1966, 10,421,763 shares	**3,473,921**	3,443,663
Capital in excess of par value	**38,977,891**	32,422,251
Retained earnings	**149,762,155**	134,582,460
	192,213,967	170,448,374
	$365,837,458	$271,448,787

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1—Principles of consolidation. All domestic and foreign subsidiaries have been included in the consolidated financial statements with the exception of (1) Lease Plan International Corp. (see Note 8 for condensed financial information), carried at equity and (2) certain recent foreign acquisitions (not significant in amount) carried at cost.

The Company's policy with respect to the inclusion of earnings of its foreign subsidiaries was changed in 1966 to a policy of reflecting in consolidated net income the current earnings of such affiliates from a prior policy of reflecting such earnings when remitted. This change had no material effect on net income in 1966. Adequate provision (including the reserve of $2,164,007 provided in prior years for such unremitted earnings, included in accrued liabilities in the accompanying balance sheet) has been made in the financial statements to give effect to the translation of foreign currencies at realistic rates. The total assets, total liabilities and net current liabilities of consolidated foreign subsidiaries and branches (other than Canadian subsidiaries) stated in terms of United States dollars were $68,200,000, $37,100,000 and $6,600,000 respectively, at December 31, 1966.

The Company has reacquired Margdave Realty Corporation from Lease Plan. Margdave's accounts, including the Montezuma sugar facility and related 4⅞% mortgage note payable, have been included in the Company's consolidated financial statements for 1966.

Certain 1965 amounts have been reclassified to conform to 1966 presentation.

Note 2—Sugar facility. The Company is constructing a beet/cane sugar facility at Montezuma, New York. This facility operated on a limited basis in the last quarter of 1966, processing the 1966 sugar beet crop. Pre-production expenses and operating losses amounting to $3,500,000 (before federal income tax benefit) incurred during the year have been charged to expense in the accompanying income statement. Cane sugar start-up operations are planned for Spring 1967 with additional beet sugar operations in the Fall of 1967. Present forecasts of operations made by management indicate that the facility will incur additional losses in 1967 but of lesser amount than in 1966.

The Company has incurred substantial capital costs in excess of its maximum guaranteed cost under the construction contract and intends to claim reimbursement for these costs, for costs related to construction contemplated in the contract and not delivered or timely completed and in addition, for consequential and other damages. In view of the plant's impaired economic value, uncertainties surrounding claims, including the possibility of protracted negotiation, arbitration and/or litigation and the magnitude of the claim when compared to the contractor's reported net assets, a provision has been made to write off excess construction costs by a charge to retained earnings of $6,240,000, representing a write off of $12,000,000 of such excess costs less estimated federal income tax benefit (charged to deferred federal income tax).

The contractor responsible for the design and construction of this facility has advised that the cost of completion will substantially exceed the presently adjusted guaranteed maximum cost. It is anticipated that unless the matter is settled by negotiation there will be arbitration to determine what, if any, portion of such excess cost is the obligation of the Company. The Company has reserved all its rights against the contractor.

A principal subcontractor has commenced two separate actions against the contractor and against the Company, respectively, seeking to collect monies alleged to be due and owing to it from the contractor and alleging further, in the case of the Company, that payment of such monies was guaranteed by the Company. Such monies are presumably for, among other things, payment of its obligations to its subcontractors. The Company has filed an answer denying the material allegations of the complaint, including the existence of any such guarantee, and the case is in preliminary stages. The principal subcontractor and a number of its subcontractors have also filed materialman's liens against the refinery property in connection with the monies alleged to be due and owing to them, which liens are generally duplicative of the aforementioned litigation claims. The Company has taken steps to contest the aforementioned liens and to discharge them of record as charges against the realty at the refinery.

Note 3—Long-term debt and retained earnings restrictions. Long-term debt as of December 31, 1966 (less current installments) consisted of the following:

4½% convertible debentures, due in 1981	$30,000,000
4⅞% mortgage note, due in semi-annual installments of $756,418 including interest to 1996	22,976,604
5¼% notes payable, due $1,250,000 annually to 1974	10,000,000
5½% note payable, due $380,000 annually to 1981	5,020,000
Other	1,396,821
	$69,393,425

PepsiCo Overseas Corporation, a wholly-owned subsidiary, issued in 1966 outside the United States, $30,000,000 of 4½% debentures due in 1981 and convertible after September 1, 1967 into 322,581 shares of the Company's capital stock at a price of $93 per share, subject to adjustment under certain conditions. In connection with this financing, the Company has recorded debt discount and capital in excess of par value in an amount ($2,850,000) equivalent to the estimated savings resulting from the lower interest rate obtained on such convertible debt when compared to the estimated higher interest rate if non-convertible debt had been issued. The resulting debt discount is being amortized over the term of the debentures.

The loan agreements contain various restrictions, including provisions relating to restrictions on the payment of dividends and the purchase of shares of the Company's capital stock. Of the consolidated retained earnings at December 31, 1966, $91,000,000 was free of such restrictions.

Note 4—Capital stock and capital in excess of par value. At December 31, 1966, 671,405 shares of the Company's authorized but unissued capital stock were reserved, 343,801 shares under restricted or qualified stock option plans, 322,581 shares for the conversion (at $93 per share) of the $30,000,000 principal amount of 4½% debentures, and 5,023 shares for conversion (at $20.90 per share) of $105,000 principal amount of 6% convertible subordinated debentures of Lease Plan.

At December 31, 1966, options were outstanding on 290,868 shares (of which 120,059 were then exercisable) having an aggregate option price of $16,091,733; the balance of 52,933 shares being available for future grants under the Company's 1964 Plan. Changes in options during 1966

were as follows: granted as to 35,067 shares having an aggregate option price of $2,471,953; exercised as to 77,863 shares having an aggregate option price of $3,468,684; and cancelled as to 14,603 shares.

The increase of $6,555,640 in capital in excess of par value is accounted for as follows:

Excess of proceeds over par value of 77,863 shares issued under stock option plans and 12,910 shares issued on conversion of Lease Plan debentures	$3,705,640
Estimated interest saving on 4½% convertible debentures (Note 3)	2,850,000
	$6,555,640

In February 1967 the Board of Directors proposed a two-for-one stock split and an increase in authorized capital stock to 30,000,000 shares, subject to shareholders' approval.

Note 5—Long-term leases and commitments. The Company and its subsidiaries are lessees under long-term leases for office space, plant and warehouse facilities expiring at various dates to 1992 having minimum aggregate annual rentals of $3,900,000 (exclusive of insurance, taxes and repairs).

At December 31, 1966 the Company and its subsidiaries were contingently liable as guarantors of loans, principally to franchised bottlers, aggregating $5,600,000.

The Company is also contingently liable for the repurchase of vending equipment acquired by franchisees, unpaid balances by them to banks in this regard being $9,700,000 at December 31, 1966.

Note 6—Federal Trade Commission. In 1963 the Federal Trade Commission issued a complaint against a subsidiary (Frito-Lay, Inc.) alleging violations of Section 7 of the Clayton Act, as amended, by reason of the acquisition of certain companies during the years 1958, 1960 and 1961. The complaint seeks to require divestiture of the assets or stock of such companies (which constitute a substantial portion of Frito-Lay's consolidated assets and operations) as going concerns and to prohibit for a period of ten years the acquisition of companies engaged in the manufacture or sale of potato chips, corn chips or pretzels. In the opinion of counsel, these charges are without legal basis. The United States District Court for the Eastern District of Texas entered an order in 1966 denying the relief sought in an action brought by Frito-Lay seeking a declaratory judgment and an injunction against the FTC. Frito-Lay appealed to the U.S. Court of Appeals for the Fifth Circuit and an order has been entered by the District Court staying all proceedings during the pendency of the appeal.

Note 7—North American Van Lines, Inc. In May 1966 the Company entered into an agreement to acquire substantially all the assets and business of North American Van Lines, Inc. in exchange for 318,409 shares of the Company's capital stock (subject to certain adjustments as provided in the agreement). The agreement has been approved by the North American shareholders and is subject to the approval of the Interstate Commerce Commission. Hearings have been held before the Commission, and a decision is now pending.

Note 8—Lease Plan International Corp. The Company's investment in Lease Plan International Corp. is carried at equity in the latter's consolidated net assets. Condensed consolidated financial statements of Lease Plan at December 31, 1966, and for the year then ended, are as follows:

CONDENSED FINANCIAL POSITION

Current assets	$ 14,516,616
Current liabilities (excluding current portion of equipment obligations)	8,494,601
	6,022,015
Revenue equipment, at cost less accumulated depreciation of $74,638,851	145,044,596
Non-current notes and accounts receivable	6,983,169
Franchises, certificates, intangibles and other assets	8,770,062
	166,819,842
Long-term debt and other liabilities:	
Equipment obligations—including $41,400,000 due within one year*	142,169,472
Other notes payable	2,488,631
Customer deposits and rental prepayments	944,795
Deferred federal income taxes	5,750,013
	151,352,911
	$ 15,466,931
Represented by:	
Common stock and capital surplus	$ 5,829,755
Retained earnings	9,249,481
Payable to PepsiCo, Inc.	387,695
	$ 15,466,931

CONDENSED STATEMENT OF
INCOME AND RETAINED EARNINGS

Operating revenues	$ 78,726,748
Operating costs and expenses (including depreciation—$39,631,431)	75,337,342
	3,389,406
Provision for federal income taxes (including reduction in deferred—$344,000)	1,305,000
Net income	2,084,406
Retained earnings at beginning of year	7,165,075
Retained earnings at end of year	$ 9,249,481

*Annual maturities of equipment obligations are—

1967—$41,400,000; 1968—$37,200,000; 1969—$28,200,000;
1970—$ 9,400,000; 1971—$ 3,300,000; After 1971—$22,700,000.

Equipment obligations are collateralized by pledge of revenue equipment and assignment of revenues to be received under customer leases and contracts. With respect to one subsidiary of Lease Plan, PepsiCo, Inc. has guaranteed $19,600,000 of equipment obligations under a revolving credit agreement expiring in 1972, which obligations are not collateralized by the pledge of revenue equipment.

PepsiCo, Inc. Directors

Herman W. Lay*†
Chairman of the Board, PepsiCo, Inc. and Chairman of the Finance Committee

Donald M. Kendall*†
President and Chief Executive Officer, PepsiCo, Inc. and Chairman of the Executive Committee

Charles Allen, Jr.†
Senior Partner, Allen & Company, Investment Bankers

Herbert L. Barnet*
Chairman of the Board, Pepsi-Cola Company

Thomas Elmezzi*
Executive Vice President, PepsiCo, Inc.

Harry E. Gould*
Chairman of the Board, Universal American Corporation, diversified manufacturer of industrial products

William B. Oliver*
President, Frito-Lay, Inc., and Vice President, Food Operations (U.S.), PepsiCo, Inc.

Herman A. Schaefer†
Vice President, Finance, PepsiCo, Inc.

James B. Somerall
President, Pepsi-Cola Company and Vice President, Beverage Operations (U.S.), PepsiCo, Inc.

Robert H. Stewart III†
Chairman of the Board, First National Bank in Dallas

Fladger F. Tannery*
Chairman of the Board, PepsiCo International and Executive Vice President, PepsiCo,Inc.

George C. Textor*
Chairman and Chief Executive Officer, Marine Midland Grace Trust Company of New York

Peter K. Warren
President, PepsiCo International and Vice President, International Operations, PepsiCo, Inc.

John D. Williamson
Senior Vice President, Frito-Lay, Inc.

**Member of the Executive Committee*
†Member of the Finance Committee

March 14, 1967

PepsiCo, Inc. Executive Offices
500 Park Avenue, New York, N. Y. 10022

Officers
Herman W. Lay, *Chairman of the Board*
Donald M. Kendall, *President and Chief Executive Officer*
Thomas Elmezzi, *Executive Vice President*
Fladger F. Tannery, *Executive Vice President*
Robert J. Abernethy, *Vice President, Manufacturing and General Services*
John R. Allison, *Vice President, Controller*
Peter J. De Luca, *Vice President, General Counsel, Secretary*
Norman Heller, *Vice President, Market Research and Planning*
Paul W. Kayser, *Vice President, Director of Industrial Relations*
Roy E. Morse, *Vice President, Research*
William B. Oliver, *Vice President, Food Operations (U.S.)*
Herman A. Schaefer, *Vice President, Finance*
James B. Somerall, *Vice President, Beverage Operations (U.S.)*
Harry E. Warren, *Vice President, Marketing*
Peter K. Warren, *Vice President, International Operations*
George Williamson, *Vice President, Treasurer*
W. Lamar Lovvorn, *Assistant Secretary*
James W. Robertson, *Assistant Secretary*
Harold E. Rome, *Assistant Secretary*
Edson E. Beckwith, *Assistant Treasurer*

Pepsi-Cola Division Executive Offices
500 Park Avenue, New York, N. Y. 10022
James B. Somerall, *President*

Frito-Lay Division Executive Offices
Frito-Lay Tower, Exchange Park, Dallas, Texas 75235
William B. Oliver, *President*

PepsiCo International Division Executive Offices
500 Park Avenue, New York, N. Y. 10022
Peter K. Warren, *President*

Lease Plan International Executive Offices
130 Steamboat Road, Great Neck, N. Y. 11022

Annual Meeting
The Annual Meeting of our Stockholders will be held at the Company's home office at 100 West Tenth Street in Wilmington, Delaware, at 2:00 P.M. (E.D.T.) Wednesday, May 3, 1967. Proxies for the meeting will be solicited by the Management in a separate Proxy Statement. This Report is not a part of such proxy solicitation and is not to be used as such.

Transfer Agents
Marine Midland Grace Trust Company of New York, New York, N. Y.
The First National Bank of Jersey City, Jersey City, N. J.
Harris Trust and Savings Bank, Chicago, Ill.
First National Bank in Dallas, Dallas, Texas
The Fulton National Bank of Atlanta, Atlanta, Ga.

Registrars
The Chase Manhattan Bank, New York, N. Y.
The First National Bank of Chicago, Chicago, Ill.
Republic National Bank of Dallas, Dallas, Texas
The First National Bank of Atlanta, Atlanta, Ga.

Auditors
Arthur Young & Company, New York, N. Y.

PEPSICO INC.